

May 15, 2012

Mr. Thomas J. Bonfield
City Manager
101 City Hall Plaza
Durham, NC 27701

RE: BCBSNC Clarification on Questions from Ms. Jones, Benefits Manager, City of Durham

Dear Mr. Bonfield:

I want to thank you and Ms. Wanda Page, Deputy City Manager, for your time today regarding the BlueCross BlueShield of North Carolina (BCBSNC) benefit proposal. During our discussion, I provided clarification on key points of our offer and I wanted to ensure you had those in writing. Specifically, I will address Ms. Ginny Jones' questions of BCBSNC following the May 10, 2012 Council Work Session.

- 1. Explain why the first amended proposal cited a 51.60% network discount but the attached excel attachment reflects a 51.30% network discount. Also, explain why we were told yesterday that we would be guaranteed a 52% network discount and why that is not contained in your proposal.**

The 51.6% in-network discount was based on data as of the time of our response to the Request for Proposal. In order to have the most current information for purposes of a discount guarantee, we re-ran the data for a more current 12-month period, which produced a 51.3% in-network discount. However, we will honor the 51.6% in-network discount and have revised the discount guarantee accordingly. We are attaching the updated discount guarantee.

As for the mention of a 52% discount, Ms. Susan Murray from BCBSNC does not recall citing that specific number as we have only referenced a 51.6% discount target for the City. I did indicate that, based on nationally recognized third party consulting benchmark data, our next closest competitor yields a network discount of less than 49%; therefore, we have greater than a 2 discount point advantage, which is worth more than \$800,000 annually in lost savings to the City of Durham, your employees, and your taxpayers. The source of the third party benchmark data is Aon Hewitt and is referred to as the Hewitt Discount Benchmarking Analysis. This tool captures all national carriers' discount information for all zip codes across the country. The City's discount comparison is based on your employees' locations.

While not part of Ms. Jones' questions, Ms. Page did ask me why our November proposal response referenced a 50.25% discount. I have clarified the source of that number – there are two ways to report discounts: (1) the discount that is earned at in-network only providers, and (2) the discount that is combined from both in-network providers (those with whom BCBSNC contracts) plus the discount generated from out-of-network providers. These two numbers combine to make up a term in the industry known as "Total Discount Measurement." Because the discount with non-contracted, out-of-network providers is often much lower than in-network

providers, the Total Discount is often lower than the in-network only discount (i.e. for the City, the Total Discount is approximately 50.25% when compared to our in-network only discount of 51.6%). Granted, this may be confusing and one may wonder why both numbers would be shared; the reason for this is to illustrate that BCBSNC is able to achieve discount savings for all claims (both in-network and out-of-network) equal to 50.25% due to our strong network of providers. This network currently covers 99% of all of the City's claims. For the purpose of the Discount Guarantee, BCBSNC used the in-network only discount target of 51.6%. I simply wanted to explain why two discount numbers may exist.

2. In lieu of an attached excel document put the information in the memo and provide a clear and concise explanation of your notes from the excel attachment. In layman terms what does it mean?

BCBSNC is offering a discount guarantee that establishes an in-network discount target (51.6% in this case) and puts administrative fees at risk based on our ability to meet that target.

There is a risk-free corridor of 3%, plus or minus, meaning that if the discount varies from target but stays within this corridor (48.6% - 51.6%), there is no payout. The reason carriers (not just BCBS) have a corridor in place is because there are no guarantees the mix of physician, inpatient hospital and/or outpatient hospital services will be the same across the entire time period. For example, let's assume an aggregate network discount of 51.6% is caused by a claims mix of 33% Inpatient, 33% Outpatient and 33% Physician charges; next, assume the Inpatient discount is 60% and the Physician discount is 40%; well, if the mix of claims switches to 20% Inpatient, 33% Outpatient and 46% Physician, the overall discount for the group will be impacted downward even though the discount we have at each of the provider types has not changed at all. This is why BCBS allows for a "buffer" in case the claims mix shifts during the plan year.

Beyond the corridor, BCBSNC puts at risk 2% of medical administration fees for every 1% discount point miss. For example, if the actual discount is 47.9%, then BCBSNC would pay a penalty to the City of 2% of medical administration fees, or \$18,553 (estimated). The greater the miss, the greater the payout to the City. The maximum payout would be 10% of medical administration fees, or \$92,763.

In addition, Ms. Jones expressed dislike of the "upside opportunity" whereby BCBS could share in the savings if the discount earned was higher than 54.6%. As shared with Ms. Jones on the evening of May 14, 2012, we are removing this provision from our guarantee. Our Discount Guarantee will only apply to a "missed" network discount.

The discount guarantee, reflecting the 51.6% target, is attached. The agreement outlines the definitions, timeframe, and how the in-network discount will be calculated.

3. Provide a clear implementation plan for your Duke solution. How would BCBSNC address the risk that "services" actually performed in a facility setting would not be paid as an office visit? For example, the visit might have been with Duke Private Diagnostic Clinic, but X-Rays might have been done at Duke. How would BCBSNC address that this may apply to all providers, not just to Duke?

We apologize for any confusion that the detail in our earlier responses has created. It was never our intention to confuse but rather we wanted to convey our flexibility in administering this provision by providing options to the City.

BCBSNC will administer the benefit for Duke Hospital owned provider offices, and any other provider offices, as an office visit copay benefit covering services associated with that office visit. In addition, we have offered a performance guarantee stating that we will achieve a 98% financial accuracy result. We are increasing the amount of fees at risk to 5% of our medical administration fees, or \$46,381.

4. Can BCBSNC positively state that it will administer true office visit co pays for all of the three benefit plan choices (Premium plan, Core plan and Basic plan) at the Duke hospital owned offices and any other hospital owned offices that a City of Durham member may visit and that a member's responsibility will only be for their corresponding co pay amount and also that facility fees will not be applied to deductible/coinsurance?

Yes, BCBSNC will administer office visit copays for each of the City's three plans for professional and facility services, as we do with any other provider.

As a general statement, I feel that we at BCBSNC have complicated this discussion of the Duke Health office visit (i.e. facility charges covered by a single copay for members), thereby making it difficult for either the Human Resources Department or the Employee Selection Committee to understand our solution. Please accept our apology for this confusion. Our solution is simple – BCBSNC is prepared to implement immediately an office visit copay to be administered as the City is requesting. BCBSNC is confident there will be no problems with our claims processing and we would point to our excellent record of claims payment as proof of our execution.

5. Indicate why BCBSNC added the caveat that the financial proposal submitted this morning assumes that BCBSNC will retain all products, including Pharmacy and Stop Loss. As you and I discussed this morning this was not addressed during our meeting on Wednesday.

The original Request for Proposal asked that we provide quotes with and without Pharmacy, which we did. The medical administration fees proposed vary depending on whether Pharmacy is included, and the same is true for our competition. Later in the process, based on discussions with the City's consultant and based on Staff's presentation to the Council Sub-Committee (which included only our bundled quote), we were given the direction that we should focus on the proposal including all coverages since the City's intention is to keep Pharmacy and Medical bundled together. Therefore, all of our financial proposals from April 19, 2012 forward have assumed that all coverages would be bundled. We simply documented this in our May 10, 2012 submission. We have the flexibility to unbundle products in the future, if the City wants.

6. Clarification of Stop Loss Contract Terms

BCBSNC would like to clarify the terms of our stop loss proposal. Our stop loss proposal is based on a "paid in 12" contract, not a 12/12 contract. In other words, any claim that is paid during the plan year, regardless of incurred date under the self-funded contract, will apply to stop loss. The competition has quoted an 18/12 stop loss contract, meaning that claims incurred during an 18 month period (3/1/2012-8/31/2013) and paid during the plan year will apply to stop loss.

The BCBSNC stop loss contract provides more comprehensive coverage than that of our competition. However, our competitor's rate is 28.8% higher than BCBSNC's rate (\$29.76 competitor vs. \$23.11 BCBSNC). The additional cost to the City would be \$215,540 for less coverage. We are not familiar with the rate of \$20.24.

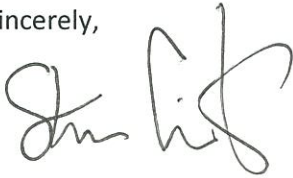
7. Confirmation of fee guarantee and wellness grant

BCBSNC guarantees our medical administration fee of \$35.62 per contract per month and our dental administration fee of \$3.02 per contract per month for three years, beginning with the 2012-13 plan year.

BCBSNC will provide a wellness grant to the City of Durham in the amount of \$50,000 for each of the next three plan years, for a total of \$150,000 over three years. Any health and wellness effort that benefits the City's employees qualifies for the wellness fund. We look forward to further discussion about wellness initiatives.

This decision is extremely important to Blue Cross, the City of Durham, its employees, and its taxpayers. For that reason, I believe it was important for me to visit with you both today and to provide this letter formalizing our clarifications. Lastly, as mentioned during our meeting, I personally will serve as the point person for all communication and questions of BCBSNC and our offer until the City Council makes its final decision. You have our undivided attention throughout your deliberations.

Sincerely,

A handwritten signature in black ink, appearing to read "Steve Crist", with a stylized flourish at the end.

Steve Crist
Vice President, Group Markets
BlueCross BlueShield of North Carolina

Cc: Ms. Wanda S. Page, Deputy City Manager, City of Durham
Ms. Virginia Jones, Benefits Manager, City of Durham
Mr. John Gasiorowski, Independent Benefit Advisors


Total Discount Measurement Guarantee Proposal
Effective 9/1/12 - 8/31/13 Paid Contract Basis
Assumptions

Number of Enrolled Employee Lives	2,701
Number of Members Enrolled	5,150
Number of Benefit Plans to be Administered	3 (Blue Options)
Membership Breakdown by Service Area	
NC	5,118
FL	6
KS	1
MD	1
NM	1
PA	2
SC	10
SD	1
TN	1
TX	1
VA	7
WA	1

Total Discount Measurement Guarantee

Savings Percent (Projected Network Discount off Billed Charges) 51.60%

Estimated Annual Administrative Fees \$927,631

(excludes Discount Performance Fees, if any)

In-Network Provider Savings Percent is:	Greater than or Equal to	But Less Than	BCBSNC Credits % of Annual Medical Admin Charges Listed Below	BCBSNC Debits % of Annual Medical Admin Charges Listed Below
		44.60%	10% (est. \$92,763)	
	44.60%	45.60%	8% (est. \$74,211)	
	45.60%	46.60%	6% (est. \$55,658)	
	46.60%	47.60%	4% (est. \$37,105)	
	47.60%	48.60%	2% (est. \$18,553)	
	48.60%	54.60%	0% (\$0)	0% (\$0)

Blue Cross and Blue Shield of North Carolina (BCBSNC) guarantees in-network provider savings on In-Network PPO Hospital and Physician claims expense for the contract period. The network savings guarantee is offered on total fee-for-service claims (Combination of Inpatient, Outpatient and Professional/Other costs), excluding Care Management Fees, Prescription drugs, and Network Access Fees, if any.

Measurement of In-Network Provider Savings Percent based on claims incurred from 9/1/12 to 8/31/13 and paid through 12/31/13.

The following definitions are applicable:

- In-Network Eligible Billed Charges = Total In-Network Billed Charges minus Total In-Network Non-eligible Charges
- In-Network Provider Savings Dollars = In-network Eligible Billed Charges minus Allowed Charges
- In-Network Provider Savings Percent = In-Network Provider Savings Dollars divided by In-Network Eligible Billed Charges

If total enrollment varies by more than 10% from the assumed, or the percent of employees enrolled by state (including other states) varies by more than 10% from the assumed, BCBSNC reserves the right to adjust the Percent of the In-Network Network Savings Guarantee, based on the expected savings by state.